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# Manifestations of FAS No. 52: Placement of the “Translation Adjustment” is Questioned

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# Manifestations of FAS No. 52

## Placement of the "Translation Adjustment" is Questioned

By Eugene L. Zieha and Orapin Duangploy

Statement of Financial Accounting Standard No. 52, Foreign Currency Translation, was issued in December, 1981.[1] Compliance was mandatory for fiscal years beginning on or after December 15, 1982. However, earlier application was encouraged and by now examples of compliance are available.

Such examples provide the first manifestations of FAS No. 52. Paralleling the idea that one picture is worth a thousand words is the idea that a sample of applications may throw some light on the seventy-eight pages of text in the statement. This paper looks at FAS No. 52 by observing the manner in which figures related to foreign currency translation appear in publicly available financial reports.

Four such manifestations of FAS No. 52 in corporate reports are given special attention. The first deals with fundamentals — double-entry bookkeeping and the comprehensive income concept. How does an increase or decrease in common stockholder equity that does not appear in the reported income of the corporation relate to the basic nature of accounting? The second views equity per share and income per share as components in the reconciliation of beginning and ending equity per share. The translation adjustment with its separate caption in the residual equity section of the statement of financial condition will be completely submerged in the single amount given for equity per share.

The third manifestation to be considered is the impact of figures generated under FAS No. 52 on traditional ratio analysis. How do you explain to a user a rate of return on equity in which the translation adjustment is included in the denominator, equity, but not in the numerator, income? And fourth, attention is given the impact of FAS No. 52 on the statement of changes in financial position. What is the interpretation of the translation adjustment, or the change therein, as a source or a disposition of whatever?

### FAS No. 52

FAS No. 52 revises the accounting and reporting requirements for recognition of foreign currency transactions and translation of foreign currency financial statements. The foreign currency transactions will, for the most part, move to a conclusion and their results will be in the income statement without specific identification. Some transactions with significantly large currency gains or losses may appear as special items on the income statement and in footnotes. However, this paper does not deal with foreign currency transactions or their appearance in the financial statements. The emphasis herein is on the translation of foreign currency financial statements and its manifestation in the published consolidated financial statements.

FAS No. 52 adopts the functional currency approach to translation. Each entity's financial statements are measured in its functional currency before translation to U.S. dollars. Under FAS No. 8, the U.S. dollar was the measuring unit for all entities.[2] Now, the measuring unit is the U.S. dollar or the foreign currency, depending on which is the functional currency. This paper considers only cases in which the foreign currency is the functional currency.

In FAS No. 52 the financial statements are translated to U.S. dollars using the current rate method. This differs from measuring exposure to currency fluctuations on monetary items only as under FAS No. 8. The current rate method addresses subsidiary statement translation from an overall entity perspective. Thus, the subsidiary's net asset position is exposed to currency fluctuations under the FAS No. 52 requirements. Translation adjustments must be reported and accumulated in a separate component of equity called Equity Adjustment for Translation.

The unrealized effects of the translation of foreign subsidiary financial statements are to be stored directly in this equity account. Changes in such unrealized gains and losses do not appear in the income statement or reside in retained earnings. The justification given in FAS No. 52 for storing the translation adjustments in this unexplained stockholders' equity account is "...(translation adjustment) is an unrealized enhancement or reduction having no effect on the functional currency net cash flows."[3] Furthermore, the FASB appears to indicate that such translation adjustments should be excluded from net income, should be included in comprehensive income, but should be treated as an equity adjustment. This inclusion in stockholder equity of an item that is excluded from income is a major point of concern herein.

## Double-Entry Bookkeeping

A.C. Littleton quotes Thomas Jones writing in 1841 as follows:

> *"The arrangement of Double Entry is based upon the following two propositions:*
>
> **Proposition I**
> *"If we can ascertain our Resources and Liabilities at any stated time, their comparison will determine the position of our affairs at that time...*
>
> **Proposition II**
> *"If we determine the position in which our affairs stood at the commencement of any period of time, and our gains and losses during that period, we can, therefore, determine our position at the end of the period...*
>
> *"So that by any possible way in which we view these two distinct and independent propositions, provided we fulfill their conditions, they must necessarily lead us to the same result."*[4]

In a continuation of this idea Littleton also discusses a German author writing in 1882. He points out that Kurzbauer indicates the importance of the union of the two classes of accounts in these words: "double-entry bookkeeping is the combination into one system of the property-bookkeeping and the results-bookkeeping of a business enterprise.[5]

W.A. Paton, in his textbook first published in 1924, takes the position:

> *"It (the income sheet) shows the course of business operation during the period from the financial standpoint, and thus accounts for the change in ownership, either favorable or unfavorable, which has resulted from such operation. That is, the periodic increase or decrease in equities, the most important financial index of the effects of business forces, is explained in more or less detail by the income sheet, assuming that this statement includes a systematic compilation of expense and revenue data."*[6]

Goldberg, writing in 1965 on the nature of accounting, continues the same idea: "What double-entry does is to combine the possibility of both measures of income and the measure of proprietorship within one system, and it is this *potentiality* that is the distinctive feature of a coherent system of double-entry bookkeeping."[7]

Countless students have been taught that they can ascertain period income by finding the change in owner's equity during the period and adjusting it for withdrawals and new investments. Many small businessmen have used such a method to determine income without the 'proof' provided by the income statement. However, tax reporting requirements have reduced reliance on the net worth approach to income calculation.

*FASB Concepts Statement No. 3,* "Elements of Financial Statements of Business Enterprises," provides a concept of comprehensive income as follows:

> *"...the change in equity (net assets) of an entity during a period from transactions and other events and circumstances from nonowner sources. It includes all changes in equity during a period except those resulting from investments by owners and distributions to owners."*[8]

But now comes FAS No. 52. Despite alternate views as to the nature of the translation, there is agreement regarding its disposition. In one place is found "...the translation adjustment is reported separately from the determination of net income. That adjustment is accumulated separately as part of equity."[9] Elsewhere the same idea is expressed as follows:

> *"...The translation adjustment for a period should be excluded from the determination of net income, reported separately, and included as a separate component of equity."*[10]

Is FAS No. 52 compatible with the comprehensive income concept of Concepts Statement No. 3? The question raised herein; it is also being raised elsewhere. Norton and Porter do so. They write, "We believe there is an inconsistency between the concept of comprehensive income and treatment of foreign currency translation items."[11]

The handling of the translation in FAS No. 52 is contrary to the basic concepts of double-entry bookkeeping, the foundation of accounting as a theoretically sound model.

Concern reaches beyond the confines of foreign currency translation. The fear is that one breakdown in the basic self-proving model would soon be used as precedent for additional deviations from time honored ideas. Accounting is not a maze of independent statistics, it is a unified system. There are many imperfections related to individual items, but the double-entry system assures that each will come to attention from two viewpoints.

Is there precedent for such direct entry of the translation adjustment to the corporate equity? Yes, there is. The 'Appraisal Surplus' that accompanied upward revaluations of assets in the 1920's is an example. But the realities of the 1930's and the test of acceptable practice caused the abandonment of this concept of upward revaluation. More seriously, there is another example waiting to come forward. Many suggestions for use of price indices or replacement costs for corporate assets would require the disposition of an offsetting credit. Residual equity has been forwarded as the resting place for this credit for many years. However, acceptance of such ideas has been consistently rejected. Is FAS No. 52 a prelude to acceptance of an even greater break with fundamentals?

## Equity Per Share

Equity Per Share (EQPS) is a financial item that is included in many corporate annual reports. When presented, it is usually included in the 'highlights' section on the first page of the report or in the multi-year financial summary. EQPS usually appears associated with earnings, both total and per share, and dividends, both total and per share. These latter figures are taken directly from the formal financial statements covered by the auditor's report. Stockholders and other annual report readers surely receive a general impression that EQPS figures have a similar standing.

In fact, the inclusion of beginning EQPS, Earnings Per Share (EPS) Dividends Per Share (DPS) and ending EQPS gives users an implication that the components of an EQPS reconciliation are being presented. But beginning EQPS plus EPS and minus DPS may not produce the ending EQPS presented in the annual report.

It has been suggested to electric utility investors that they use these

**TABLE 1**
**R. J. Reynolds Industries**
**Statement of Reconciliation of Equity Per Share**
**Jan. 1, 1983 — Dec. 31, 1983**

| | |
|---|---|
| EQPS 1/1/83 (per annual report $42.33) | $42.33 |
| Plus Earnings per Share | 7.25 |
| | $49.58 |
| Less Dividends per Share | (3.05) |
| | $46.53 |
| Plus Equity Transfers in Connection with Acquisition of Debentures, Preferred Stock, Subordinated Debentures, and Other | .04 |
| | $46.57 |
| Less Foreign Currency Translation Adjustment | (.46) |
| EQPS 12/31/83 (per annual report $46.11) | $46.11 |

**TABLE 2**
**Scoville, Inc.**
**Statement of Reconciliation of Equity Per Share**
**Dec. 26, 1982 — Dec. 25, 1983**

| | |
|---|---|
| EQPS 12/26/82 (per annual report $17.82) | $17.82 |
| Plus Earnings per Share | 2.53 |
| | $20.35 |
| Less Dividends per Share | (1.52) |
| | $18.83 |
| Plus Equity Transfer in Connection with options exercised, Preferred Converted, Public Issuance, Issuance in Acquisition, and Debt Exchange | 1.70 |
| | $20.53 |
| Less Foreign Currency Translation Adjustment | (.65) |
| EQPS 12/25/83 (per annual report $19.88) | $19.88 |

figures for a simple test. Compute an expected EQPS and compare it with the actual EQPS. A lower actual than expected EQPS gives strong suspicion of stockholder dilution. This usually occurs when new shares are issued at less than current EQPS. It was further suggested that they write corporate management and ask for an explanation of this difference. Luckily foreign subsidiaries are not found among regulated electric utilities.

FAS No. 52 has further complicated this unresolved problem by adding a new feature to the equity section of the Balance Sheet. The total given for common stockholders' equity is the sum of Capital Stock at Par, Premium on Capital Stock, Retained Earnings and Translation Adjustment. EQPS is usually calculated by dividing this total common stockholders' equity by the number of common shares outstanding at the balance sheet date. The word 'usually' appears because there may be a few cases in which the total is adjusted. One possible adjustment is for the difference between balance sheet figures and liquidation value of certain preferred stock. In addition, some financial publications use a 'book value' for common stock for which intangibles have been deducted from the total before dividing by the number of shares.

The Translation Adjustment did not appear on the Balance Sheet until FAS No. 52 was adopted. It can be expected that analysts will continue to divide total common equity by shares outstanding given the mode of presentation in statements reviewed to date. The companies have done so in computing the EQPS they show in their annual reports.

More sophisticated audiences are being asked to do more than a simple test. A full Reconciliation of Changes in EQPS is being proposed and promoted. Research has indicated a sizeable number of line items that may appear in such a reconciliation. The Translation Adjustment will be one. It will be much harder to explain to users than such items as income, dividends, and equity transfer due to issuance of new shares at other than EQPS.

An illustration may make this clearer than further verbage. Statements of Reconciliation of Equity Per Share and the worksheets from which they were prepared are provided for two of the companies whose annual reports were reviewed for this paper. These materials appear in Tables 1 through 4. A firm decision has not been made as yet as to how the Translation Adjustment should be handled in the proposed Statement of Reconciliation of EQPS. It is made as a final item and its effect is prorated on a relatively simple basis in these examples. The important things are that the Translation Adjustment is necessary for the reconciliation and that it is a significant item for these companies. This is definitely a manifestation of FAS No. 52.

## Ratio Analysis

Ratio analysis of financial data is an established feature of corporate financial management, credit granting decisions and investment portfolio supervision. Users of annual reports have a continuing interest in this tool and, therefore, in the accounting data that is its raw material. Moreover,

## TABLE 3

### Worksheet for Reconciling Equity Per Share
### (Dollars in millions except per share)

| R.J. Reynolds Ind., Inc. | # Shares | Total Dollars | Average Per Share | $ New Stockholders | $ Old Stockholders | Per Share Old Stockholders |
|---|---|---|---|---|---|---|
| Balance 12/31/82 | 112,596,534 | $4,766 | $42.328 | $ — | $4,766 | $42.328 |
| Common Shares Transactions | 676,674 | 35 | 51.724 | 35 | — | — |
| Equity Transfer A | — | — | — | −6 | +6 | .056 |
| Sub-Total | 113,273,208 | 4,801 | 42.384 | 29 | 4,772 | 42.384 |
| Income | — | 819 | — | 3 | 816 | 7.252 |
| Dividend | — | − 345 | — | −2 | −343 | −3.050 |
| Equity Transfer B | — | — | — | +2 | −2 | −.017 |
| Sub-Total | 113,273,208 | 5,275 | 46.569 | 32 | 5,243 | 46.569 |
| Current Year Translation Adjustment | — | 52 | — | −1 | −51 | .459 |
| Balance 12/31/83 | 113,273,208 | 5,223 | 46.110 | 31 | 5,192 | 46.110 |

## TABLE 4

### Worksheet for Reconciling Equity Per Share
### (Dollars in millions except per share)

| Scovill, Inc. | # Shares | Total Dollars | Average Per Share | $ New Stockholders | $Old Stockholders | Per Share Old Stockholders |
|---|---|---|---|---|---|---|
| Balance 12/26/82 | 9,454,824 | $168,457 | $17,817 | $ — | $168,457 | $17.817 |
| Options Exercised | 164,050 | 2,562 | 15.617 | 2,562 | — | — |
| Preferred Converted | 20,292 | 185 | 9.117 | 185 | — | — |
| Public Issuance | 1,700,000 | 46,971 | 27.630 | 46,971 | — | — |
| In Acquisition | 260,000 | 6,151 | 23.658 | 6,151 | — | — |
| Debt Exchange | 537,831 | 13,891 | 25.828 | 13,891 | — | — |
| Total Issuances | 2,682,173 | 69,760 | 26.009 | 69,760 | — | — |
| Equity Transfer A | — | — | — | −17,116 | +17,116 | +1.810 |
| Sub-Total | 12,136,997 | 238,217 | 19.627 | 52,644 | 185,573 | 19.627 |
| Income | — | 27,246 | — | 3,350 | 23,896 | +2.527 |
| Dividend | — | −16,311 | — | −1,940 | −14,371 | −1.520 |
| Equity Transfer B | — | — | | +1,006 | −1,006 | −.106 |
| Sub-Total | 12,136,997 | 249,152 | 20.528 | 55,060 | 194,092 | 20.528 |
| Current Year Translation Adjustment | — | −7,880 | — | −1,741 | −6,139 | −.649 |
| Other | — | −27 | — | −6 | −21 | −.002 |
| Balance 12/25/83 | 12,136,997 | 241,245 | — | 53,313 | 187,932 | 19.877 |

## TABLE 5
### Return on Shareholders' Equity

**Cluett, Peabody & Co., Inc. & Subsidiaries**

| As Reported: | | (In thousands) | |
|---|---|---|---|
| Shareholders' Equity 1/1/83 | | $215,806 | |
| Shareholders' Equity 12/31/83 | | 229,309 | $445,115 |
| Simple Average | | | 222,558 |
| Net Income 26,829/222,558 = 12.05% | | | |
| Adding Back Translation Adjustments of 6,485 and 14,031 to Equity: | | | |
| | 1/1/83 | 222,291 | |
| | 12/31/83 | 243,340 | 465,631 |
| Simple Average | | | 232,816 |
| Net Income 26,829/232,816 = 11.54% | | | |
| or | | | |
| Deducting Translation Adjustment For Year of 7,546 from Net Income | | | |
| | 1/1/83 | 215,806 | |
| | 12/31/83 | 229,309 | 445,115 |
| Simple Average | | | 222,558 |
| Net Income 26,829 − 7,546 = 19,283 | | | |
| 19,283/222,558 = 8.66% | | | |

## TABLE 6
### Return on Shareholders' Equity

**Datapoint Corporation & Subsidiaries**

| As Reported: | | (In thousands) | |
|---|---|---|---|
| Shareholders' Equity 8/1/82 | | $326,150 | |
| Shareholders' Equity 7/31/83 | | 329,963 | $656,113 |
| Simple Average | | | 328,057 |
| Net Income 8,077/328,057 = 2.46% | | | |
| Adding Back Translation Adjustments of 5,269 and 11,541 to Equity: | | | |
| | 8/1/82 | 331,419 | |
| | 7/31/83 | 341,504 | 672,923 |
| Simple Average | | | 336,462 |
| Net Income 8,077/336,462 = 2.40% | | | |
| or | | | |
| Deducting Translation Adjustment For Year of 6,356 from Net Income | | | |
| | 8/1/82 | 326,150 | |
| | 7/31/83 | 329,963 | 656,113 |
| Simple Average | | | 328,057 |
| Net Income 8,077 − 6,356 = 1,721 | | | |
| 1,721/328,057 = .525% | | | |

ratios are frequently presented in the corporate reports. They are not within the financial statements that are reviewed by the auditor; but they do appear in the same document and are prepared from the same accounting figures.

What effect will compliance with FAS No. 52 have on these ratios? Financial analysts use a set of perhaps twelve to sixteen relatively standard ratios. Limited space herein does not allow a detailed review of each such ratio. Attention will be directed primarily to one ratio, rate of return on stockholders' equity, which appears frequently in corporate annual reports. Some general comments will be made on the others without detailed supporting explanation. Worksheet presentations in Tables 5 through 8 will establish background for the comments.

Two approaches can be taken. One is to compare ratio results under FAS No. 52 with those under FAS No. 8. This can be extended to include predecessor translation methods such as current/non-current or monetary/non-monetary. But FAS No. 52 is the standard and evaluating it in terms of past practices is not practical in a limited presentation. The second approach, to be followed here, is to evaluate FAS No. 52 alone with concern for possible weak points or internal inconsistencies.

Users of financial ratios do not see the detailed breakout of statement components. These are submerged in one final percentage. This is especially true in the ratio, rate of return on stockholders' equity, that is being examined. The current rate translation method scatters increased or decreased asset and liability figures throughout the balance sheet which are incorporated in the consolidated figures. The net currency translation change appears in the cumulative Translation Adjustment that is presented (by most companies) as a separate line item in the stockholders' equity section of the balance sheet. The current year translation 'change' does not appear in the income statement.

Return on average stockholders' equity, as presented in annual reports, is calculated by dividing net income to common stockholders by the average stockholder's equity. A simple average, one half the sum of beginning and ending equity, is reasonable unless there are unusual equity transactions.

A simple test was performed on the data in several available annual reports. Three rates of return were calculated. The first uses the data presented in the report and gives a result compatible with the figure presented elsewhere in the annual report. The second step recognizes that the Translation Adjustment is not in the income figure. Compatibility is achieved by removing it from the equity figure. Most current translation adjustments are negative. Their removal raises the stockholders' equity figure. This, in turn, results in a smaller calculated return on stockholders' equity. However, in the samples used the difference was insignificant.

The third calculation also recognizes the Translation Adjustment is not in the income figure and adds it algebraically to income. Calculation with this data provides again a lower rate of return than that shown in the statements. However, the difference in this case is considerably larger because a change in the profit figure is much more significant than a change in the net asset (equity figure).

Tests with hypothetical data confirm the empirical evidence above. A negative translation adjustment occurs as a result of a decline in a foreign currency. The rate of return under FAS No. 52 is then greater than it would have been if the decline were completely ignored or completely recorded on a full double-entry basis.

On the other hand, if the foreign currency strengthens, the published rate of return under FAS No. 52 will be below that which would have been shown if the equity denominator and the income numerator in the calculation were compatible.

The analysis and the limited empirical review of published data indicates that for many companies this may not be a significant difference. However, two comments are in order. One is that including the adjustment in one part of a calculation but not in the other is akin to the traditional adding of apples and oranges.

The other is that this difference indicates only a small leak in the accounting dam. Leaks may get bigger and others may join them. Particularly interesting is that one of the companies whose statements were reviewed has a single equity adjustment account

## TABLE 7
### Return on Shareholders' Equity

**Petrolane Incorporated and Subsidiaries**

| | | | |
|---|---|---|---|
| As Reported: | | (In thousands) | |
| Shareholders' Equity 10/1/82 | | $511,513 | |
| Shareholders' Equity 9/30/83 | | 451,571 | $963,084 |
| Simple Average | | | 481,542 |
| Net Loss (34,609)/481,542 = (7.19%) | | | |
| Adding Back Translation Adjustments of 3,836 and 4,836 to Equity: | | | |
| | 10/1/82 | 515,349 | |
| | 9/30/83 | 456,407 | 971,756 |
| Simple Average | | | 485,878 |
| Net Loss (34,609)/485,878 = (7.12%) | | | |
| or | | | |
| Adding Translation Adjustment For Year of 1,000 to Net Loss | | | |
| | 10/1/82 | 511,513 | |
| | 9/30/83 | 451,571 | 963,084 |
| Simple Average | | | 481,542 |
| Net Loss (34,609) + (1,000) = (35,609) (35,609)/481,542 = (7.39%) | | | |

## TABLE 8
### Return on Shareholders' Equity

**Rockwell International Corp. and Consolidated Subsidiaries**

| | | | |
|---|---|---|---|
| As Reported: | | (In millions) | |
| Shareholders' Equity 10/1/82 | | $2,097.3 | |
| Shareholders' Equity 9/30/83 | | 2,367.3 | $4,464.6 |
| Simple Average | | | 2,232.3 |
| Net Income 389.1/2,232.3 = 17.43% | | | |
| Adding Back Translation Adjustments of 89.8 and 89.9 to Equity: | | | |
| | 10/1/82 | 2,187.1 | |
| | 9/30/83 | 2,457.2 | 4,644.3 |
| Simple Average | | | 2,322.2 |
| Net Income 389.1/2322.2 = 16.76% | | | |
| or | | | |
| Deducting Translation Adjustment For Year of 0.1 from Net Income | | | |
| | 10/1/82 | 2,097.3 | |
| | 9/30/83 | 2,367.3 | 4,464.6 |
| Simple Average | | | 2,232.3 |
| Net Income 389.1 − .1 = 389 389/2,232.3 = 17.43% | | | |

that included both the foreign currency translation adjustment and an adjustment for the decline in value of long-term investments in equity securities.

## Changes in Financial Position

The Statement of Changes in Financial Position (SCFP) has undergone a long period of development to become a part of the formal financial presentation. It is a tool, that along with the Income Statement and the Equity Statement explains the changes from one Balance Sheet to the next. Accounting Principles Board Opinion No. 19 establishes the authoritative position relative to this statement. FAS No. 52 adopts the all financial resources concept and other requirements as specified in APB Opinion No. 19.

However, FAS No. 52 fails to specify whether the explanation of the change in financial position is in terms of the functional currency or the U.S. dollar. Has a change in financial position occurred when balance sheet amounts change because of the translation process? If the financial statement measurements exist only in terms of the functional currency, then translation is the process of expressing such measurements. In this case, the implementation of the change in financial position should be in terms of the foreign currency. All items of the foreign currency statement of changes in financial position will be translated at the exchange rate on the balance sheet date. There will not be a translation adjustment to account for on the SCFP.

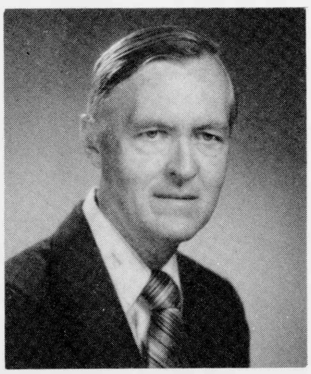
The situation is different if the objective of the translated SCFP as viewed by FAS No. 52 is in terms of the U.S. dollar. Any significant changes in balance sheet items resulting from changes in the exchange rates should be reported. APB Opinion No. 19 supports the all financial resources concept. Any transaction that gives rise to important changes in financial position should be shown on the translated SCFP even though working capital or cash is not affected directly. Such transactions are not a factor in measuring the net change in funds but they must be disclosed because they affect the structure of the firm's assets and equities. Consequently, a strict adherence to the all financial resources concept should fully disclose the translation adjustments.

FAS No. 52 fails to specify how to disclose the translation adjustments. But, it appears that to be consistent with APB Opinion No. 19 requirements, the translation adjustments should be reported as both a source and use of funds. However, APB Opinion No. 19 permits some flexibility and use of judgment in meeting the stated objectives of the SCFP. At the same time, FAS No. 52 gives very little guidance regarding its impact on the SCFP.

Empirical evidence available to date shows how companies have elected voluntary compliance with FAS No. 52 report translation adjustments. It is recognized that the election of voluntary compliance introduced a significant bias into the accumulated data. However, it is the best available data as compliance was mandatory beginning with fiscal periods starting after December 15, 1982.

There is a second problem with this data which time will correct. The profession is in a transient period regarding compliance with FAS No. 52. Many companies must make cumulative adjustments relative to prior years' data. It is particularly difficult to relate such prior years' adjustments, the changeover from FAS No. 8 to FAS No. 52, to the SCFP. Companies which have their initial adjustment in a prior year will have a more simple adjustment in the succeeding year. They will be moving from the transient state conditions into steady state conditions. This will give further insight into the impact of FAS No. 52 on the SCFP.

An unscientific review of available corporate annual reports revealed a wide diversity in the handling of FAS No. 52 data in the SCFP. Some companies show both a source and use of funds that are, in effect, the result of the translation adjustment. Others show what could well be construed as uses as negative sources. The effect of the translation adjustment does not appear in some SCFP's even though its inclusion in equity establishes the need for an offsetting amount. Perhaps it is submerged in "other." Another approach shows the effect of the translation as a balancing figure independent of both sources and uses. The handling of the FAS No. 52 translation in the SCFP is complicated by the fact that there are many different company concepts of the SCFP.



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## Conclusion and Recommendations

The introduction of FAS No. 52 is having many manifestations in the financial reports of companies that have foreign subsidiaries whose functional currency is the foreign currency. These manifestations appear in the balance sheet, the equity statement and in the statement of changes in financial position. They, furthermore, impact the income statement by their absence from it.

Review to date of these manifestations gives rise to two questions. The first asks whether the Translation Adjustment on the balance sheet should be removed from the equity section of this statement. Its presence there raises questions as to whether it conflicts with basic concepts of double-entry bookkeeping. In addition, does it cause problems to users with an interest in ratio analysis or with a desire for a better understanding of equity per share and its changes?

Could the Translation Adjustment be moved to another position on the balance sheet? One possibility is a separate section between liabilities and shareholders' equity for such unrealized items. Or perhaps this separate section could go below the equity section. Another possibility is the viewing of the translation adjustment on the balance sheet as a valuation account to be added or subtracted, with appropriate explanation, from total assets or groups of assets. No position is taken herein at the present time beyond a call for a further study of this aspect of FAS No. 52.

A simple approach that would not change the basic position of FAS No. 52 relative to this item does exist. A sub-total of Capital Stock, Premium on Capital Stock and Retained Earnings could be entitled "Shareholders' Equity Before Translation Adjustment for Foreign Currency Changes." Further discussion could establish this subtotal as the figure to be used in ratio analyses and calculation of equity per share.

It is further proposed that additional attention be paid to the placement of the Translation Adjustments on the Statement of Changes in Financial Position. Recognition that any decision here must be related to a better agreement on the nature of this statement is important. Ω

### NOTES

[1]Financial Accounting Standards Board, "Foreign Currency Translation," Statement of Financial Accounting Standards No. 52 (FASB, December 1981).

[2]Financial Accounting Standards Board, "Accounting for the Translation of Foreign Currency Transaction and Foreign Currency Financial Statements," Statement of Financial Accounting Standards No. 8 (FASB, October 1975).

[3]FASB, FAS No. 52.

[4]Littleton, A.C., "Accounting Evolution to 1900" (American Institute Publishing Company, 1933).

[5]Ibid.

[6]Paton, W. A., "Accounting" (MacMillan Company, 1924).

[7]Goldberg, Louis, "An Inquiry Into The Nature of Accounting" (American Accounting Association, 1965).

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